

ARIZONA TAX NEWS



Jane Dee Hull, Governor

Mark Killian, Director

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E-Mail Your Questions

If you have a question that you cannot find the answer for, our Technical Assistance personnel may prove useful to you. We will gladly respond to any e-mail technical tax inquiry with the exception of specific account inquiries. All inquiries will be responded to within two working days.

E-mail your question to:
TaxpayerAssistance@revenue.state.az.us

In the interest of maintaining confidentiality, DOR can not respond to inquiries that include a Social Security number, FEIN, TPT or W/H number, or other specific taxpayer identifiers.

Arizona Taxpayer Bill of Rights Ruling TBR 00-1 Summary

ISSUE:

Whether certain tanning facility operators understated their transaction privilege tax obligations as a result of an extensive misunderstanding or misapplication of the tax laws and, if so, what is the affected class of taxpayers and what are the terms of the closing agreements.

DISCUSSION:

On May 5, 1999, the Director of the Department issued Transaction Privilege Tax Ruling 99-5 ("Ruling") that expressed the Department's position regarding the taxability of tanning facilities. The Ruling stated that "income derived by tanning facility businesses and other establishments from their customer's use of tanning equipment is subject to transaction privilege tax under the personal property rental classification." The Department will allow a reasonable time for the Ruling to be disseminated to the affected taxpayers, and for the affected taxpayers to begin remitting the required transaction privilege tax.

The Department received a letter from a taxpayer requesting that the Assistant Director of the Transaction Privilege Tax Division ("Division") determine that as a result of the same extensive misunderstanding or misapplication of the tax laws more than 60 percent of the businesses operating tanning facilities in Arizona unintentionally or inadvertently failed to report or pay transaction privilege tax on certain revenues received. The Division researched the issue and found that less than 10% of the tanning facilities were remitting transaction privilege tax on the revenues received for the use of tanning machines. As a result of this finding, a Notice of Public Hearing (Notice) was

published in the *Arizona Capitol Times*, a newspaper of general circulation, on March 31, 2000. The Notice stated that a public hearing would be held on April 27, 2000, at 1:30 p.m. at the Industrial Commission, 800 W.

Washington, Phoenix, Arizona. The class of taxpayers was defined as those entities who have receipts from engaging in the business of providing tanning equipment for use by others. Letters, similar to the Notice, were also sent to all known businesses that operated tanning facilities. The Notice provided that copies of relevant, non-confidential documents could be obtained and reviewed from 8:00 a.m. to 5:00 p.m. at the reception desk in the lobby of the Revenue Building located at 1600 West Monroe, Phoenix, Arizona. It also indicated that if additional information was needed, the taxpayer could contact Robert Ridenour at (602) 542-4656, or by writing him at 1600 W. Monroe, Phoenix, Arizona 85007.

On April 27, 2000, at 1:30 p.m. in the Industrial Commission Amphitheater, a public hearing was held, pursuant to the Taxpayer Bill of Rights, A.R.S. § 42-2056, regarding the failure of tanning bed operators to file returns and pay transaction privilege tax.

John D. Sylvester, Problem Resolution Officer for the Department of Revenue and designated hearing officer, presided at the hearing (which was recorded), announced that under A.R.S. § 42-2056 the Department of Revenue may enter into closing agreements with the members of a class of taxpayers if the department determines that, as a result of the same extensive misunderstanding or misapplication of the tax laws, more than 60 percent of the persons in the affected class of taxpayers failed to properly account for their taxes. In addition, he stated that the Department of Revenue defined the proposed class of affected taxpayers as those businesses that have receipts from engaging in

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*** REMINDER ***

FOR NON-EFT TPT FILERS

To avoid a delinquency, postmark your September 2000 TPT return no later than October 25th or deliver to DOR no later than October 30, 2000.

June Summary of General Fund Revenues

	June 2000	Fiscal Year Total
Individual Income Tax		
Net Collections	\$223,455,875	\$1,911,617,932
Percent Change *	27.8%	8.8%
Corporate Income Tax		
Net Collections	\$98,175,872	\$523,181,563
Percent Change *	(12.5%)	(4.1%)
Transaction Privilege, Severance & Use Taxes		
Net Collections	\$247,172,117	\$2,817,525,828
Percent Change *	11.1%	9.8%
Total Big Three Tax Types		
Net Collections	\$568,803,864	\$5,252,325,323
Percent Change *	11.6%	7.9%

() Decrease from same month last year.

* Percent change from same month last year.

Individual Income Tax

Individual Income Tax Receipts

May 2000	June 2000	June 1999	Change
Gross Collections	\$80,134,600	\$70,011,149	14.5%
Withholding	201,450,895	170,647,698	18.1%
Refunds	(26,653,704)	(37,519,471)	(29.0%)
Urban Rev Sharing	(31,475,916)	(28,359,221)	11.0%
Net Collections	\$223,455,875	\$174,780,155	27.8%
Fiscal Year Total	(99/00)	(98/99)	Change
Gross Collections	\$817,545,878	\$758,925,529	7.7%
Withholding	2,253,705,597	2,056,475,429	9.6%
Refunds	(781,922,555)	(717,771,496)	8.9%
Urban Rev Sharing	(377,710,989)	(340,310,656)	11.0%
Net Collections	\$1,911,617,932	\$1,757,318,80	58.8%

TAX CALENDAR

OCTOBER 2000

Due Date		For Period Ending
09	Columbus Day (observed)	All State Offices Closed
16	Income Tax Returns:	6/30/00
	Form 120: Corporation	
	Form 140: Individual	
	Form 141: Fiduciary	
	Form 165: Partnership	
16	Form 120: Corporation with Automatic Extension	12/31/99
16	Form 120S: S Corporation	7/31/00
16	Exempt Organizations	5/31/00
	Form 99: Annual Information Return	
	Form 99T: Unrelated Business Income	
16	Form 120ES: Estimated Tax Payment, Corporation	
	First Installment	6/30/01
	Second Installment	4/30/01
	Third Installment	1/31/01
	Fourth Installment	10/31/00
20	Form TPT-1: Transaction Privilege Tax: September Monthly Filers and Quarterly Filers	9/30/00
20	Bingo: Financial Reports	9/30/00
20	Luxury Tax: Various Forms	9/30/00
25	EFT Form TPT-1 and Payment: Transaction Privilege Tax: September Monthly Filers	9/30/00
31	Withholding Tax: Form A1-QRT	9/30/00
31	Unclaimed Property Reports: All entities except Life Insurance Cos. (Report accounts dormant for 5 years as of June 30th of the report year, except utility refunds, which are dormant for 2 years)	

Withholding Tax Payment Information:

If the average amount of Arizona income taxes withheld in the preceding four calendar quarters **exceeds** \$1,500 the employer must make its Arizona withholding payments to the Department of Revenue at the same time as the employer is required to make federal withholding deposits.

If the average amount of Arizona income taxes withheld in the preceding four calendar quarters **does not exceed** \$1,500 the employer must make its Arizona withholding payments to the department on a quarterly basis.

The Arizona Tax News is a monthly publication of the Arizona Department of Revenue. Information contained herein is of a general nature and is not designed to address complex issues in detail. Taxpayers requiring information concerning a specific tax matter should contact the appropriate office. This newsletter is available in alternative formats upon request by calling the telephone number shown below. Subscription information may be obtained from the Community Outreach & Education Section, 1600 W. Monroe, 6th floor, Phoenix, AZ 85007, or call Tony Manzo at (602) 542-3062 or toll free 1 (877) 863-0655.

Gilbert Change in City Tax Code Effective: Retroactive to July 1, 2000

The Mayor and Town Council of the Town of Gilbert have passed Ordinance No. 1271. Ordinance No. 1271 allows Construction Contracts entered into prior to the rate increase effective July 1, 2000 to be taxed at the rate in effect prior to July 1, 2000.

Construction Contracts entered into and signed prior to July 1, 2000 are taxed at the rate of **1%** and must be reported using **Code GB9**.

Fountain Hills Change in City Tax Code Effective: November 1, 2000

The Mayor and Common Council of the Town of Fountain Hills have passed Ordinance 00-12. Ordinance 00-12 increases the Town Privilege Tax Rate from 1.2% to **1.6%** effective November 1, 2000. The **Privilege tax** will continue to be reported using **CODE FH** and the **Use tax** will continue to be reported using **CODE FH2**. The privilege tax rate increase affects the following classifications:

- Amusements.
- Construction Contracting.
- Job Printing.
- Manufactured Buildings.
- Timbering and Other Extraction.

- Publishing.
- Hotels.
- Rental of Real Property.
- Rental of Tangible Personal Property.
- Restaurants and Bars.
- Retail sales.
- Telecommunications
- Transporting for Hire.
- Utilities and Use Tax.

For those contacts entered into prior to November 1, 2000 (**pre-existing contracts**), the tax rate will remain at 1.2% and be reported using **CODE FH9**.

Sierra Vista Change in City Tax Code Effective: November 1, 2000

The Mayor and City Council of the Town of Carefree passed Ordinance No. 1119. Ordinance 1119 deletes Local Option B. Deleting Option B reserves out Sec. 280-Transactions with governmental agencies, and establishes paragraph (n) of Sec.465-Retail Exemptions, relating to sales made directly to the federal government. Sales made directly to the Federal government are exempt to the extent of:

(1) One hundred percent (100%) of the gross income derived from retail sales made by a manufacturer, modifier, assembler, or repairer.

(2) Fifty percent (50%) of the gross income derived from retail sales made by any other person.

IRS Interest Rates for Over and Under Payments

The Internal Revenue Service has announced that interest rates for the calendar quarter beginning October 1, 2000 will remain the same for both underpayments and overpayments. Therefore, our interest rate will remain the same at 9% for underpayments and will also remain at 9% for overpayments.

Under the Tax Reform Act of 1986, the rate of interest is determined on a quarterly basis. The overpayment / underpayment rates are now the same as we have conformed to the 1999 I.R.C., passed during the 1999 Legislate Session.

2000 Income Tax Legislative Summary

HB 2060: Agricultural Preservation District Land, Tax Credit (CH. 267)

Creates a refundable income tax credit for individuals and corporations for donating land or development rights to land to an agricultural preservation district. The amount of the credit is equal to the appraised value of the property if ownership is conveyed to the district or the difference between the appraised value of the undeveloped land and the appraised value of the land for development purposes if

the taxpayer conveys the development rights to the district. The total credits in any single district cannot exceed \$33,000 in any calendar year. The credit is available for taxable years 2001 through 2005. Also, creates an addition to Arizona gross income for amounts deducted for conveying property or development rights to a district.

HB 2226: Tuition Tax Credit, Handicapped Preschoolers (CH. 394)

Amends A.R.S. §43-1089 to include preschools for handicapped students in the definition of qualified schools for purposes of the credit for contributions made to a

school tuition organization. Applies to taxable years beginning from and after December 31, 2000.

HB 2245: Reviser's Technical Corrections; 2000 (CH. 32)

Contains, in part, technical corrections that relate to individual and corporate income tax. The provisions

correct defective enactment and errors in statutory cites.

HB 2329: Vehicle License Tax, Corporate Tax Rates (CH. 48)

- Changes the amount of vehicle license tax that is provided to the state general fund to aid school finance from 23 cents to 6 cents and changes the amount to the state highway fund from 14 cents to 10 cents.
- Reduces the corporate income tax rate to 6.968 percent effective for taxable years beginning from and after December 31, 2000. (This effective date was amended by SB 1424.)
- Repeals the year 2000 conditional (trigger) enactment.

HB 2442: Technology Training; Tax Credit (CH. 239)

Provides a refundable income tax credit to individuals and corporations for providing qualified technology skills training to employees.

The amount of the credit is the lesser of 50% of the training costs or \$1,500 per employee per taxable year. A taxpayer may not claim a credit for more than twenty employees. The maximum credit for all corporate taxpayers is \$2.5 million per year. The maximum credit for all individual taxpayers is \$2.5 million per year.

The credit is effective for taxable years beginning from and after December 31, 2000 and ending before January 1, 2006.

To receive this credit a taxpayer must apply to the Department of Commerce on or before January 15 of the year following the calendar year in which the credit is claimed. If applications exceed the \$2.5 million threshold, Commerce must proportionately reduce the amount of credit for each taxpayer.

HB 2451: Tax Credit; School Site Donation (CH. 334)

Provides income tax credits for individuals and corporations that donate real property and improvements to a school district or charter school for use as a school or as a site for the construction of a school.

The amount of the credit is 30% of the fair market value of the property donated and is in lieu of a charitable deduction for the donation.

To qualify for the credit, the property must be located in Arizona. In addition, the property must be subject to certain deed restrictions and, in the case of a donation to a charter school, a lien in the amount of the allowable tax credit adjusted by the average change in the GDP price deflator for each calendar year since donation, not exceeding 12.5% more than the allowable credit.

Taxpayers are allowed a 5-year carryover for unused credits.

School districts may sell donated property; however, the proceeds must be used for capital projects. Charter schools that receive donated property are required to pay the State Treasurer the amount of the tax credit allowed in the event of the financial failure of the charter school or if the charter school fails to establish a school on the property or provide instruction to pupils within certain time frames.

The lien recorded with the title to the property donated to a charter school is extinguished on the earliest of the following:

- Ten years after the lien is recorded.
- On payment to the State Treasurer the amount of the allowable tax credit.
- On conveyance of the property to a school district.
- On enforcement and satisfaction of the lien by the State Treasurer's Office.

The bill is effective for taxable years beginning from and after December 31, 2000.

HB 2459: Income Tax Subtraction; Holocaust Reparations (CH. 286)

Amends ARS § 43-1022 and adds a new ARS § 43-1030 to provide an income tax subtraction for distributions made to a taxpayer for the taxpayer's persecution or for the persecution of the taxpayer's ancestor by Nazi Germany or any other axis regime for racial, religious, or political reasons. ARS § 43-1030 also provides a subtraction for items of income that are attributable to, derived from, or related to assets that were stolen or hidden from or lost to a taxpayer who was persecuted by Nazi Germany or any other axis regime for racial, religious, or political reasons. The

subtraction applies to the taxpayer who is the first recipient of any distribution or recovered asset.

ARS § 43-1030 also provides that any income received by a taxpayer for the taxpayer's persecution or for the persecution of the taxpayer's ancestors by Nazi Germany or any other axis regime shall not be included for the purposes of any state program that uses income as an eligibility requirement.

This legislation applies retroactively to taxable years beginning from and after December 31, 1999.

SB 1220: Tourism and Sports Authority (CH. 372)

Income Tax Summary:

Adds a new A.R.S. § 43-209 that requires the following:

- Requires the department to adopt and enforce rules for collection of income tax on the income earned for services performed in Arizona by professional athletes and employees of professional sport franchises.
- Requires every professional football franchise organization that is domiciled in Arizona to provide the department with the federal identification number of each resident and nonresident employee who performed services in Arizona during the calendar year. The numbers are to be provided on or before December 31 and a penalty of five dollars is provided for failure to provide a number.
- Requires the department to separately account for and report to the state treasurer, on or before March 31, the total aggregate net income tax revenues collected on income from all sources during the preceding calendar year from the following:
 - Any professional football franchise organization that is domiciled in Arizona.
 - Resident and nonresident employees of any professional football franchise organization domiciled in Arizona. This includes all income reported on a joint return by married individuals and the income of an employee's spouse that is reported on a separate return.
- Amends ARS § 43-1116 to provide that each month, beginning July 2001 the state treasurer is required to transmit to the Tourism and Sports Authority the greater of one-twelfth of the amount reported by the Department under ARS § 43-209 or \$292,000 per month for first 12 month period (increased by an additional eight per cent for each subsequent twelve-month period).
- Contains a conditional repeal, if the surcharge is not approved by the voters, from and after November 30, 2000.

SB 1369: Income Tax Credit; Character Education (CH. 313)

Amends ARS § 43-1089.01 to create an individual income tax credit of up to \$200 for paying fees or for making a cash contribution in support of a character development instruction program or for the support of extracurricular

activities. The credit would be in lieu of a charitable contribution deduction and could be carried forward for up to 5 years. Applies to taxable years beginning from and after December 31, 2000.

SB 1493: Estate Tax; Filing Extension (CH. 265)

Amends ARS § 42-1107 to provide that the Department

may grant reasonable cause filing extensions for Arizona estate tax returns.

SB 1531: Spaceport; Launch Site; Exemption (CH. 359)

Adds a deduction under the prime contracting classification for gross proceeds of sales or gross income derived from a contract entered into for the construction of a launch site, as defined in 14 code of federal regulations, part 401.5.

Also adds a deduction from the tax base under the prime

contracting classification for gross proceeds of sales or gross income derived from a contract entered into for the construction of a domestic violence shelter that is owned and operated by a nonprofit charitable organization that has qualified under section 501(c)(3) of the internal revenue code.

Arizona Transaction Privilege Tax Ruling

TPR 00-2 Summary

ISSUE:

The transaction privilege tax implications of prime contracting activities that include the installation of machinery, equipment and other tangible personal property qualifying for deduction from tax under A.R.S. § 42-5061(B), under Laws 1996, Chapter 319 (S.B. 1280), and under Laws 1998, Chapter 90 (S.B. 1323), effective January 1, 1999. This ruling is applicable for tax periods beginning January 1, 1999.

RULING:

The deduction under A.R.S. § 42-5075(B) (9) is for the gross proceeds of sales or gross income attributable to the contractor's *purchase price* of machinery, equipment or other tangible personal property that is exempt from or deductible from transaction privilege and use tax according to the statute.

Effective January 1, 1999, with or without an agency agreement, the amount a prime contractor receives from a project owner as reimbursement for the purchase of *qualified* machinery, equipment or other tangible personal property is excludable from the prime contractor's gross contracting revenue before computing the tax base for the project under A.R.S. § 42-5075(B)(7) and (9).

Under A.R.S. § 42-5061(B)(7) a prime contractor can deduct the gross proceeds of sales or gross income of a contract to install, assemble, repair or maintain qualified machinery and equipment and other tangible personal property that does not become a permanent attachment to real property when computing its tax base. However, the portion of any contracting activity that consists of the development of, or modification to, real property in order to facilitate the installation, assembly, repair, maintenance or removal of the machinery, equipment or other tangible personal property may not be deducted.

Under A.R.S. § 42-5075(B)(9) the gross

proceeds of sales or gross income derived from a contract to permanently install, assemble, repair or maintain qualified machinery, equipment or other tangible personal property is includable in a prime contractor's tax base under the prime contracting classification.

EXAMPLES:

A contractor is performing actions that constitute an "improvement to real property."

If the contractor purchased, with or without an agency agreement, machinery or equipment that was exempt under A.R.S. § 42-5061(B) which was not permanently attached to the realty, then under A.R.S. § 42-5061(B)(7) the contractor may deduct the labor portion of the contract from the contractor's gross income except for that portion of any contracting activity which consists of the development of, or modification to, real property in order to facilitate the installation, assembly, repair, maintenance or removal of machinery, equipment or other qualifying tangible personal property. The equipment cost will not be included in the gross income of the contractor.

If the contractor purchased machinery or equipment that was exempt under A.R.S. § 42-5061(B), with or without an agency agreement, which was permanently attached to the realty, then under A.R.S. § 42-5061(B)(9) the contractor cannot deduct the labor portion of the contract from the contractor's gross income. The equipment cost will not be included in the gross income of the contractor.

*For more information
see the complete TPR 00-2 at the
Arizona Department of Revenue Website:
www.revenue.state.az.us*

"Effective January 1, 1999, with or without an agency agreement, the amount a prime contractor receives from a project owner as reimbursement for the purchase of qualified machinery, equipment or other tangible personal property is excludable from the prime contractor's gross contracting revenue before computing the tax base for the project under A.R.S. § 42-5075(B)(7) and (9)."

(Continued from page 1)

the business of providing tanning equipment for use by others. All relevant portions of the notice of public hearing were read. He also disclosed that the Department of Revenue anticipated a decision within the next 60 days and that a tax ruling and closing agreements would be forthcoming if the department determined that the affected class qualified under the provisions of A.R.S. § 42-2056.

Robert Ridenour, Director's Office of Tax Policy and Legal Support, testified that, after the receipt of a letter from a taxpayer requesting relief under A.R.S. § 42-2056, the Division researched the issue and found that there was greater than 60% of the affected taxpayers not complying with the taxing statute, as expressed by the Department in Transaction Privilege Tax ("TPR") Ruling 99-5. He further stated that the public hearing was to determine the reason or reasons for the non-compliance. The hearing officer heard testimony from taxpayers and taxpayer representatives. They testified that they had concluded that the activity was a service business. The hearing officer also heard testimony from Robert Ridenour, who testified that research by the Division also revealed that taxpayers who failed to comply had done so because they had concluded that they were engaged in a service business. The hearing officer found that the testimony was relevant and credible, and that a substantial misunderstanding therefore existed.

RULING:

The Hearing Officer found that more than sixty percent of the

tanning business operators had understated their Arizona transaction privilege and use tax liability by failing to report or pay transaction privilege tax on certain revenues through an extensive misunderstanding or misapplication of the tax laws and that the class of affected taxpayers is those businesses that have receipts from engaging in the business of providing tanning equipment for use by others.

At the recommendation of the Hearing Officer and in the interest of fair dealing and equity, the Department will provide to members of the affected class an opportunity to enter into closing agreements under which tax, penalties and interest otherwise due will be waived in accordance with A.R.S. § 42-2056 for tax periods prior to August 31, 1999, subject to the applicable statute of limitations. Tanning facility operators who correctly reported and paid transaction privilege tax on revenues may also enter into closing agreements for the same tax periods, and the Department will refund the amount of tax, penalties and interest paid as a result of their proper reporting and payment of tax. Taxpayers entering into the closing agreements must in the future properly account for and pay any transaction privilege taxes due. Tanning facility operators that want to avail themselves of this Ruling must enter into closing agreements within sixty (60) days of receiving notice of this Ruling.

For information concerning closing agreements, contact Robert Ridenour, Department of Revenue, at (602) 542-4656, Ext. 7671 or by facsimile at (602) 542-5005.